

August 9, 2003

Mr. Tom Carter
Operations Manager
Western Area Power Administration
Sierra Nevada Region
Parkshore Drive
Folsom, California

Dear Mr. Carter:

The City of Santa Clara, doing business as Silicon Valley Power (SVP) respectfully submits comments in response to the Western Area Power Administration's filing in the Sierra Nevada Region Federal Register Notice dated June 12, 2003 (FR Doc. 03-1585) regarding post-2004 operating decisions and the contemplated formation of a Federal Control Area (FCA).

SVP believes that the FCA offers significant benefits not only to Western's municipal customers but also to the California marketplace and the Western Region as a whole. California's municipal utilities, which constitute Western's customer base in California, are almost the only financially healthy and creditworthy market participants remaining in the state. The munis are now best positioned to invest in the vitally needed physical infrastructure that is an essential prerequisite to a properly functioning power market. Among California's utilities and suppliers of power, the munis have created the most successful business model, featuring consistently reliable service as well as positive financial results. Through prudent resource development, bilateral supply contracts, cash management and above all, focus on serving load economically, the munis have consistently achieved superior operating performance, low rates and customer satisfaction. Supporting the California munis therefore offers the best prospects of reviving the wholesale power market in California, and the establishment of the FCA is an important step towards providing this support.

Of particular importance is the way in which establishing the FCA will help shield this one healthy segment of the market in California from the ills of the other segments, which are largely the result of the disarray now reigning in California politics and in the leaderless, dysfunctional, mutually conflicted plethora of state agencies. For the market to recover and become whole and dynamic once more, it is important that its best performers not be dragged down to the level of its failures. Once again, SVP believes that establishing the FCA is a positive step towards maintaining the health of this high-performing market segment and enabling it to restore a vibrant, seamless wholesale energy marketplace to not just California but all of the Western Region.

Among the benefits to the Western Region as a whole, SVP believes, contrary to the CAISO's assertions, that the FCA actually will facilitate access to the surplus capacity of public-sector transmission systems in Northern California and more effectively control costs. Also, since Western is subject to oversight by the Federal Energy Regulatory Commission, SVP is assured that Western's management of the system will conform to strict rules of open access. The FCA will help overcome the present indirection and stasis of California's regulatory bodies by providing a stable, reliable system administration for these transmission assets. Instituting the FCA is also consistent with the trend towards vertical reintegration of utilities in California, which itself reflects an acknowledgment that the vertically integrated operations of utilities offer the cleanest and most efficient business model. In fact, SVP feels that this trend is likely to render the existing system operator structure irrelevant and obsolete, particularly as California joins with the rest of the Western Region in an improved administration of generation and transmission resources.

SVP is confident that Western will use the funds it receives from its customers to serve them cost-effectively, consistently with its long prior record of solid performance in this regard. SVP notes that this confidence, which is shared with so many other customers of Western, is founded on a realistic assessment of relative risks and costs with respect to establishing the FCA. SVP further notes that since customers will support Western's administration of the system out of their own pockets, there is no added cost or risk to the Department of Energy or the state of California in approving the new control area. Costs have always been important to SVP and its ratepayers. It is our contention that the benefits of forming a Western FCA strongly outweigh the costs despite the CAISO's arguments to the contrary.

SVP's detailed comments as to the specifics of Western's proposal follow.

Sincerely,

James H. Pope
Director of Electric Utility

COMMENTS OF THE CITY OF SANTA CLARA
dba SILICON VALLEY POWER
in re PROPOSED FEDERAL CONTROL AREA

Background Information

The City of Santa Clara, doing business as Silicon Valley Power (SVP), provides retail electricity service to our customers in the heart of Silicon Valley. Our industrial customers include a "Who's Who" of the top United States companies in the valley, including Intel's World Headquarters, Advanced Micro Devices, National Semiconductor, and many more. SVP is a member of the Transmission Agency of Northern California (TANC) and part owner of the 500-kV California Oregon Transmission Project (COTP). As a Preference Power customer in Western's Sierra Nevada Division, SVP has an interest in the 500-kV PACI transmission line. Reliable, attractively priced power is very important to all of our customers. Western's power deliveries are an important part of our power portfolio, which also includes a number of renewable resource projects and other power resources from throughout the Western United States.

SVP commends Western for its exploration of a Federal Control Area (FCA) option. This option has the strongest potential to protect Western's customers from continuously rising costs, endless tariff amendments and further risks inherent in the behavior of the current control area operator. SVP favors control area operations that enhance reliability, provide transparency and flexibility, avoid anomalous and disastrous market outcomes and serve customers at reasonable and predictable costs. We believe a Federal Control area would achieve all of the above objectives.

SVP supports Western's stated qualitative criteria

SVP strongly endorses Western's stated decision criteria as filed in the Federal Register Notice dated June 12, 2003 (FR Doc.03-1585):

- Flexibility
- Certainty
- Durability
- Operating Transparency
- Cost Effectiveness.

These stated criteria serve to highlight what is so wrong in today's market and what was so right in our longer-term history. The City of Santa Clara has operated its own electric utility for 107 years, and has always focused on reliability and attractive rates as leverage for the City's economic health and development. Despite recent industry trends, SVP is financially sound and strongly creditworthy.

Reliability and Cost-Effectiveness

The objective of having control areas is to enhance system reliability. Western has demonstrated, through its successful operation of four other control areas in the Western Electric Coordinating Council (WECC) region, that it can operate reliable and cost-effective control areas with a

minimum of procedural changes over time. SVP expects that Western will apply the same expertise in forming and operating a Northern California control area. The formation of a Federal Control Area is clearly the best way for Western to maintain consistency with Federal policy regarding the operation and control of the Central Valley Project.

Price uncertainty remains an enormous problem in dealing with the CAISO. Given the excessive complexity of the CAISO's billing and settlements process, and the contingent nature of many charge types, it is nearly impossible for SVP to manage the costs of doing business with the CAISO. After no less than 55 amendments to the CAISO tariff in 5 years, we wonder how many more amendments will increase and reallocate costs. In 2003 we are still litigating CAISO charges that go all the way back to its inception in 1998!¹ The interminably cumulative work load that results from this chaotic settlement process detracts not only from our own efforts, but is certain to adversely affect the CAISO's management of the grid. This situation is unacceptable to SVP, and compels us to pursue appropriate avenues to maintain our financial strength and our focus on customer service, and shield ourselves from the CAISO's uncontrollably rising costs. Western's formation of a control area is one great step forward towards price certainty and cost control.

Sanctity of Existing Contracts

SVP resolutely supports honoring existing contracts and agreements. SVP believes that contracts governing the rights and obligations of load-serving entities must be maintained intact in their fundamentals over time. Western has consistently observed this principle of the durability of contracts in doing business. Western's record of using and honoring contracts for its power and transmission services is a compelling reason to support Western's initiative towards establishing its own control area. Western has repeatedly and consistently demonstrated its ability to operate reliable, cost effective, and durable control areas. Western has a long and distinguished record of serving a diverse range of customers in a satisfactory and cooperative manner.

By contrast, the CAISO has adopted an essentially adversarial posture towards California's municipal utilities and has undertaken to abrogate and undermine their rights and obligations under existing contracts unilaterally through its unrelenting barrage of tariff amendments. The CAISO's governance structure, with state control of its Board of Directors, and the fact that the assets the CAISO controls serve principally the state's three major investor-owned utilities, creates an unavoidable conflict of interest. The CAISO's anomalous position compels it to act against the interest of public power in California, with consequent harm to the ratepayers of precisely those market participants who have performed most successfully and most honorably for the last century and more, and most notably in the chaos and dysfunction of California's electricity "deregulation" experiment.

Transmission Rights and Congestion Management

SVP believes that transmission should be allocated and utilized based upon physical firm transmission rights as these have historically been understood and exercised. With contractually secured physical rights, there is no need for costly congestion management schemes, multiple markets, or fictitious congestion, nor to degrade the definition of "firm transmission rights" to something less than the historically understood meaning, as the CAISO has repeatedly

¹ ER00-565 SCS case.

undertaken to do. The CAISO's efforts to abolish the consensus meaning of firm transmission rights and its management practices have resulted, *inter alia*, in detrimental manipulation of congestion not only by market participants, but by the CAISO itself.

SVP also believes that Western's operation of another control area would reduce, if not avoid altogether, the problems of excessive complexity experienced under the CAISO regime. Western's successful operation of its existing four control areas has been accompanied by consistent, timely and relatively trouble-free scheduling procedures and settlement processes, presenting a marked contrast to the convolutions and delays in CAISO settlements.

Physical Infrastructure and Seams Issues

SVP supports having the California Oregon Transmission Project (COTP) placed in the proposed FCA. SVP believes that with Western as the control area operator, COTP participants would enjoy increased transfer capabilities at reduced costs. We believe that seams issues would be more efficaciously resolved between two federal control areas, i.e. the Bonneville Power Administration's existing control area and a Western Federal Control Area, than between the BPA control area and the CAISO. It makes great sense to have the California Oregon Intertie (COI) in control of a Western FCA since about 80 percent of the COTP and the PACI is owned by TANC and Western.

Western's ownership of its existing 500-kV AC Intertie line from Malin to Round Mountain substations, with a transfer capability of 1600 MW, plus the ownership by TANC, Western and other municipals of nearly all of the COTP, the newest 500-kV AC Intertie to the Northwest, positions Western ideally to manage these segments of the Western Region's grid. Since these two lines form two thirds of the California Oregon Intertie (COI), it is therefore logical for Western to include the COI in its control area, rather than conceding these facilities to the CAISO.

The legislative history of the Intertie also clearly supports an all-Federal connection between Western and the Bonneville Power Administration (BPA) system. We believe that Congressional requirements for the Western 500-kV line can best be met by having Western be the path operator for the COI. Appropriate operating procedures with the CAISO can be developed to ensure coordinated operations and ease the CAISO's concerns regarding seams.

Such an arrangement will only enhance, not impair, the reliability of the interconnected systems. In the Northwest there are already multiple control areas and various Intertie owners and rights. BPA has done a good job of coordinating these rights and we would expect Western to do a similarly good job in California.

Metered Subsystem Agreement Issues

Thus far, SVP has been able to serve its customers through our Metered Subsystem Agreement (MSSA) with the CAISO, but we are concerned about our ability to continue doing so, so long as the CAISO persists in its proliferation of tariff amendments. Although SVP's MSSA contains statements that the MSSA will prevail in the event of conflicts with the CAISO tariff, other portions of the MSSA allow for amendments to the CAISO tariff and other unilateral CAISO filings that can effectively change the terms of the MSSA. The CAISO habitually files its tariff changes without much stakeholder input and without allowing adequate time for comment, as in the case of its latest MD02 filings of July 21, 2003. In consequence of these latter provisions,

SVP has had to constantly fight to protect our MSSA from these potentially adverse tariff changes.

A parallel cause of frustration for SVP is the CAISO's MD02 process, which is another source of threats to SVP's contractual rights. Through its MD02 initiative, the CAISO has neglected to provide assurance that key components of the MSSA will not be dismantled. Despite participation by SVP and other MSSA parties in the CAISO stakeholder process, the CAISO's MD02 filings have, in many cases, lacked the necessary details and assurances that important MSSA provisions will remain in place. In its promulgation of MD02, instead of signaling its long-term acceptance of MSSA protections for MSSA parties, the CAISO continues to urge MSSA parties to accept the same treatment as other market participants. We continue to comment to ensure that our MSSA maintains sufficient control and flexibility over our resources.

Summary

In conclusion, SVP believes that, given the demonstrated attitude of the CAISO, the MSSA vehicle is insufficient over time to satisfy any of the five criteria earlier enunciated by Western: flexibility, certainty, durability, operating transparency and cost effectiveness. SVP has had to expend excessive amounts of time, effort, and legal fees defending and staving off challenges to our rights under the MSSA, without assurance of success. The bottom line is that the protections which our MSSA provides for our customers lack survivability, despite our efforts to work out issues and memorialize our understanding with the CAISO within the MSS context. We believe we will find more certainty and durability in another control area, and we encourage Western to proceed with the formation of its own control area in Northern California.